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IN THE

Supreme Court of the United States

No. [redacted]132

OCTOBER TERM, 1961

HARRIET B. SAWYER,

Petitioner,

vs.

PIONEER MILL COMPANY, LTD., a corporation (plus the individual defendants),

Respondents.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

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PIONEER MILL COMPANY, LTD., a corporation (plus the individual defendants),

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Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

Petitioner prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals entered in the above-entitled case on March 14, 1962; petition for rehearing denied on April 5, 1962.

Citations for Opinions Below.

The opinion of the District Court of Hawaii, printed in Appendix B hereto, *infra*, page 3 is reported in 190 Fed. Supp. 21. The opinion of the Circuit Court of Appeals, printed in Appendix B hereto, *infra*, page 8, is not yet reported.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered on March 14, 1962, Appendix B, page 8, *infra*. Rehearing was denied on April 5, 1962. The jurisdiction of this Court is invoked under 28 U. S. C. Sec. 1254(1).

Question Presented.

Petitioner sought to enjoin respondent directors from voting fraudulently-obtained proxies in favor of merging respondent corporation in which petitioner was an investor. Before any corporate vote was taken, the District Court dismissed petitioner's action for want of jurisdiction on the ground that the solicitation of proxies for a merger was not a "purchase or sale" as defined by the Securities Exchange Act of 1934. On appeal, respondents' motion was dismissed upon a showing that the proxies had been subsequently voted, the Court holding that petitioner could not proceed further with her action because the purported successor corporation had not been made a party defendant in the original complaint.

The question thus presented is whether the effective enforcement of the federal anti-fraud statutes protecting securities investors has been undermined and nullified by the failure of the courts below to decide if:

A. A merger is a "purchase and sale" within the meaning of Section 10b of the Securities Exchange Act?

B. Consummation of a merger effected through violation of said section deprives a Federal Court of jurisdiction to grant appropriate relief?

Statutes Involved.

The statutory provisions involved are Section 10(b) of the Securities Exchange Act of 1934 (15 U. S. C. 78j); Rule 10b-5 (17 C. F. R. 240, 10b-5) thereunder and Section 27 of said Act (15 U. S. C. 78a). They are printed in Appendix A, *infra*, pages 1, 2.

Statement.

Petitioner, as a shareholder of respondent Pioneer Mill Company, Limited ("Pioneer"), brought this action in the United States District Court for the District of Hawaii against Pioneer and its officers and directors to enjoin them from holding a special meeting of the stockholders of Pioneer, from continuing to use or transmit to stockholders of Pioneer an allegedly false and misleading proxy statement and from voting any proxies already obtained by the use of such statement [R. 8, 9].[1] The proxies were solicited and the meeting was to be held for the purpose of approving a merger agreement between Pioneer and American Factors, Limited ("American") whereby stockholders of Pioneer would exchange each of their shares for one-and-one-tenth shares of American [R. 4, 5]. The complaint, as amended in open court, alleged that the stockholders' approval of the exchange was solicited by false and misleading statements in violation of Section 10(b) of the Securities Exchange Act of 1934 (15 U. S. C. 78j) and Rule 10b-5 (17 C. F. R. 240, 10b-5) thereunder and invoked the jurisdiction of the court below under Section 27 of that Act (15 U. S. C. 78aa) [R. 3, 5, 30].

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[1] "R." refers to pages of the Record.

The complaint alleged that American is the owner of 57.48% of the outstanding stock of Pioneer, and that six of the ten directors of Pioneer are either directors or officers of American [R. 4, 5]. According to the complaint, on October 10, 1960, respondents distributed to stockholders of Pioneer in connection with the proposed exchange of shares a proxy statement that was false and misleading in grossly undervaluing the land holdings of Pioneer by listing them at acquisition cost instead of at their fair market value, in failing to disclose the existence and value of certain claims in favor of Pioneer arising out of the abuse of trust by American as agent and controlling stockholder of Pioneer [R. 5-8] and in inflating the value of American by listing as a non-current receivable sums owed to it by a subsidiary which would probably never be paid [R. 8]. The allegations of the complaint must, of course, be assumed to be true for the purposes of a motion to dismiss.

On motion of respondents, the District Court on November 28, 1960 dismissed the complaint for lack of jurisdiction over the subject matter on the ground that the solicitation of proxies was "not for the purpose of effecting a purchase or sale of any security" within the meaning of Section 10(b) and Rule 10b-5 thereunder [R. 33]. The court also denied a motion made by appellant to amend the complaint to add, in the alternative, a prayer for rescission of the merger contract if approved at the stockholders' meeting [R. 32].

On the following day, November 29, 1960, a special stockholders' meeting of Pioneer took place at which the contested proxies were voted by respondents enabling the merger to be approved by the required 75%

of the outstanding stock. On December 12, 1960, formal judgment was entered against appellant [R. 23, 24] and on December 21, 1960, appellant filed her notice of appeal from said judgment [R. 36].

On January 6, 1961, the merger agreement was executed by the appellees and the officers of American Factors, Limited and approved by the State Treasurer of Hawaii.

After a hearing *en banc* the court below dismissed without prejudice Petitioners appeal on March 14, 1962 stating Appendix B, *infra*, page 11.

> "In short, since the purpose was to prevent the meeting, or the use of the proxies at the meeting, since both of these things have happened, and since the present action is not an appropriate vehicle for an attack upon the merger, the action has become moot (*Sobel v. Whittier Corp., et al.*, 6 Cir., 1952, 195 F. 2d 361; *Kelaghan v. Industrial Co., et al.*, 1 Cir., 1954, 211 F. 2d 134; *Fink v. Continental Foundry & Machine Company*, 7 Cir., 1957, 240 F. 2d 369)."

Reasons for Granting Writ.

1. The question presented is of importance in the administration of the federal laws protecting securities investors.

The Securities and Exchange Commission, by amicus brief filed in this case in the court below, urged that a federal court has jurisdiction to rescind a consummated corporate transaction effected by means of violations of the anti-fraud provisions of the federal securities laws (27th Annual Report of the S. E. C. [1961] p. 50). The problem has recently received nation-wide

attention from legal scholars[2] and arises in an area of constantly-increasing public involvment.[3]

Section 27 of the Securities Exchange Act vests the United States district courts with exclusive jurisdiction over "all suits in equity and actions at law brought to enforce any duty or liability created" by the Act. This necessarily includes petitioner's action brought to enjoin alleged violations of Section 10(b) and Rule 10b-5 thereunder. See, for example, the decisions of the Ninth Circuit in *Matheson v. Armbrust*, 284 F. 2d 670 (1960), cert. den. 365 U. S. 870; *Errion v. Connell*, 236 F. 2d 447 (1956); *Fratt v. Robinson*, 203 F. 2d 627 (1953). These cases make clear that in order to make the control of securities transactions "reasonably complete and effective," as specifically contemplated by Section 2 of the Exchange Act, Section 10(b) creates a duty to refrain from the practices defined as manipulative or deceptive devices by Rule 10b-5. See particularly *Fratt v. Robinson, supra*, 203 F. 2d at 632. The duty created is necessarily a federal duty; the breach of this duty creates a federal liability in behalf of the persons for whom the rules were enacted. *Cf. Matheson v. Ambrust, supra*, 284 F. 2d at 673.

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[2]Loss "Securities Regulations" 2d Ed., p. 2032; 967-71;
3 Boston College L. Rev. (1961), 58, see particularly footnote 63 on p. 67 referring to the instant case;
9 U. C. L. A. L. Rev. (Jan. 1962) 232;
40 Texas L. Rev. (1962), 405;
151 Duke L. J. (1962), see footnote 14 on p. 154;
75 Harv. L. Rev. (Jan. 1962) 637;
62 Columbia L. Rev. (Feb. 1962) 375.

[3]Proxy solicitations for mergers of listed companies alone increased from 112 in 1957 (p. 76 of 23rd Annual Report of S. E. C.) to 197 in 1961 (p. 72 of 27th Annual Report of S. E. C.)

A suit to enjoin violations of the Act, as an action in equity, makes available all the equitable remedies of a district court to afford complete justice by moulding "each decree to the necessities of the particular case." *Hecht Co. v. Bowles*, 321 U. S. 321, 329 (1944). In *Bell v. Hood*, 327 U. S. 678, 684 (1946), the Supreme Court noted:

> "Moreover, where federally protected rights have been invaded, it has been the rule from the beginning that courts will be alert to adjust their remedies so as to grant the necessary relief."

2. The decision of the court below is believed to be erroneous and in conflict with applicable decisions of this Court.

In its decision dismissing appellant's appeal as moot, the court below relied solely upon *Sobell v. Whittier Corp.* (C. A. 6), 195 F. 2d 631; *Kelaghan v. Industrial Trust Co.* (C. A. 1), 211 F. 2d 134; and *Fink v. Continental Foundry and Machine Co.* (C. A. 7), 240 F. 2d 369, but these were all diversity actions brought on behalf of corporations through stockholders suing derivatively. Only questions of private corporation law were involved, not the supremacy of a federal statutory design to protect securities investors. Recognition should be given to the distinction between (a) diversity actions brought by corporations (through a stockholder) to prevent being absorbed by a merger, and (b) actions brought by securities investors to obtain federal protection under Section 10b, *supra*, against misuse of the mails which would convert their individual investments to other corporate securities of lesser value. When a corporation disappears, the plaintiff suing in its behalf loses his standing to sue. But if the mails have been

used to cheat a securities investor, the special protection provided by Congress should not vanish simply because one of the parties defendant has switched corporate identities during the pendency of an appeal.

The reach of federal statutes cannot be avoided by parties litigant who shed their corporate skins. *United States v. Trans-Missouri Freight Assn.* (1887), 166 U. S. 290, 307-310.

A defendant who has been notified of the pendency of a suit seeking an injunction against him acts at his peril and is subject to a continuing judicial power which can restore the *status quo* even though a temporary injunction has been denied. *Jones v. S. E. C.* (1935), 298 U. S. 1; *Porter v. Lee* (1946), 328 U. S. 246, 251; *Texas and New Orleans R.R. Co. v. Northside Belt R.R. Co.* (1928), 276 U. S. 475, 479.

3. The decision of the court below in the instant case conflicts with the decision of the Eighth Circuit Court of Appeals in *Dyer v. S. E. C.* (1959), 266 F. 2d 33, where the Court held at pp. 46-47:

> "Doubtless, there can be questions of such a nature or incidence in relation to a proxy solicitation that their administrative significance can become moot from a holding of the stockholders meeting. But we are satisfied that questions too can exist, as in the present situation, which are of such a character or consequence that they cannot properly be regarded as having become fixed or dissolved or otherwise rendered inoperative by the holding of the meeting.
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> "Relatedly, and as a matter of preventing legal frustration, it is evident that, unless the situation is

so dealt with, it will be impossible practicably for any affected party (whether petitioners, management, or the other stockholders) ever to obtain on a proxy-solicitation question the judicial review provided for by the statute, so as to be able to get such a situation acceptedly settled or legally stabilized. Experience in the two situations which have now been before us shows that it is physically impossible, in a proxy-solicitation controversy of such character and length as these two have been, to get the proceedings for review perfected and subject to hearing and disposition, between the time of the action of the Commission and the date of the corporation's annual meeting, unless a stay is granted, for which there is no occasion in the ordinary situation."

4. The decision of the court below in the instant case also conflicts with the decision of the Sixth Circuit in *Dann v. Studebaker* (1961), 288 F. 2d 201, where the court held that, at the very least, a shareholder was entitled to declaratory relief in a case where the corporate transaction complained of had been consummated.

Conclusion.

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

ROBERT W. KENNY,

Counsel for Petitioner.